must not be used. In the negotiation documentation, the contracting officer need not explain assignment of the normal value, but must address conditions that justify assignment of other than the normal value.

[64 FR 51473, Sept. 23, 1999, as amended at 65 FR 12485, Mar. 9, 2000]

1815.404–471–2 Performance risk.

(a) *Risk factors*. Performance risk addresses the contractor's degree of risk in fulfilling the contract requirements. It consists of three risk factors:

(1) Technical—the technical uncertainties of performance;

(2) Management—the degree of management effort necessary to ensure that contract requirements are met; and

(3) Cost control—the contractor's efforts to reduce and control costs.

(b) *Risk factor weighting, values and calculations*. A weighting and value is assigned to each of the risk factors to determine a profit/fee objective.

(c) *Values*. The normal value is 6 percent and the designated range is 4 percent to 8 percent.

(d) *Evaluation criteria for technical risk factor*. (1) In determining the appropriate value for the technical risk factor, the contracting officer shall review the contract requirements and focus on the critical performance elements in the statement of work or specifications. Contracting officers shall consider the—

(i) Technology being applied or developed by the contractor;

(ii) Technical complexity;

(iii) Program maturity;

(iv) Performance specifications and tolerances;

(v) Delivery schedule; and

(vi) Extent of a warranty or guarantee.

(2) *Above normal conditions indicating substantial technical risk*. (i) The contracting officer may assign a higher than normal value in those cases where there is a substantial technical risk, such as when—

(A) The contractor is either developing or applying advanced technologies;

(B) Items are being manufactured using specifications with stringent tolerance limits;

(C) The efforts require highly skilled personnel or require the use of state-of-the-art machinery;

(D) The services or analytical efforts are extremely important to the government and must be performed to exacting standards;

(E) The contractor's independent development and investment has reduced the Government's risk or cost;

(F) The contractor has accepted an accelerated delivery schedule to meet the Government's requirements; or

(G) The contractor has assumed additional risk through warranty provisions.

(ii) The contracting officer may assign a value significantly above normal. A maximum value may be assigned when the effort involves—

(A) Extremely complex, vital efforts to overcome difficult technical obstacles that require personnel with exceptional abilities, experience, and professional credentials;

(B) Development or initial production of a new item, particularly if performance or quality specifications are tight; or

(C) A high degree of development or production concurrency.

(3) *Below normal conditions indicating lower than normal technical risk*. (i) The contracting officer may assign a lower than normal value in those cases where the technical risk is low, such as when the—

(A) Acquisition is for off-the-shelf items;

(B) Requirements are relatively simple;

(C) Technology is not complex;

(D) Efforts do not require highly skilled personnel;

(E) Efforts are routine; or

(F) Acquisition is a follow-on effort or a repetitive type acquisition.

(ii) The contracting officer may assign a value significantly below normal. A minimum value may be justified when the effort involves—

(A) Routine services;

(B) Production of simple items;

(C) Rote entry or routine integration of Government-furnished information; or

(D) Simple operations with Government-furnished property.

(e) *Evaluation criteria for management risk factor.* (1) In determining the appropriate value for the management risk factor, the contracting officer shall review the contract requirements and focus on the critical performance elements in the statement of work or specifications. Contracting officers shall—

(i) Assess the contractor's management and internal control systems using contracting office information and reviews made by contract administration offices;

(ii) Assess the management involvement expected on the prospective contract action; and

(iii) Consider the degree of cost mix as an indication of the types of resources applied and value added by the contractor.

(2) *Above normal conditions indicating substantial management risk.* (i) The contracting officer may assign a higher than normal value when the management effort is intense, such as when—

(A) The contractor's value added is both considerable and reasonably difficult; or

(B) The effort involves a high degree of integration and coordination.

(ii) The contracting officer may justify a maximum value when the effort—

(A) Requires large-scale integration of the most complex nature;

(B) Involves major international activities with significant management coordination; or

(C) Has critically important milestones.

(3) *Below normal conditions indicating lower than normal management risk.* (i) The contracting officer may assign a lower than normal value when the management effort is minimal, such as when—

(A) The program is mature and many end item deliveries have been made;

(B) The contractor adds minimum value to an item;

(C) The efforts are routine and require minimal supervision;

(D) The contractor fails to provide an adequate analysis of subcontractor costs; or

(E) The contractor does not cooperate in the evaluation and negotiation of the proposal.

(ii) The contracting officer may assign a value significantly below normal. A minimum value may be assigned when—

(A) Reviews performed by the field administration offices disclose unsatisfactory management and internal control systems (e.g., quality assurance, property control, safety, security); or

(B) The effort requires an unusually low degree of management involvement.

(f) *Evaluation criteria for cost control risk factor.* (1) In determining the appropriate value for the cost control risk factor, the contracting officer shall—

(i) Evaluate the expected reliability of the contractor's cost estimates (including the contractor's cost estimating system);

(ii) Evaluate the contractor's cost reduction initiatives (e.g., competition advocacy programs);

(iii) Assess the adequacy of the contractor's management approach to controlling cost and schedule; and

(iv) Evaluate any other factors that affect the contractor's ability to meet the cost targets (e.g., foreign currency exchange rates and inflation rates).

(2) *Above normal conditions indicating substantial cost control risk.* (i) The contracting officer may assign a value higher than normal value if the contractor can demonstrate a highly effective cost control program, such as when—

(A) The contractor has an aggressive cost reduction program that has demonstrable benefits;

(B) The contractor uses a high degree of subcontract competition; or

(C) The contractor has a proven record of cost tracking and control.

(3) *Below normal conditions indicating lower than normal cost control risk.* (i) The contracting officer may assign a lower than normal value in those cases where the contractor demonstrates minimal concern for cost control, such as when—

(A) The contractor's cost estimating system is marginal;

(B) The contractor has made minimal effort to initiate cost reduction programs;

(C) The contractor's cost proposal is inadequate; or

(D) The contractor has a record of cost overruns or the indication of unreliable cost estimates and lack of cost control.

[64 FR 51473, Sept. 23, 1999]

1815.404–471–3 Contract type risk and working capital adjustment.

(a) *Risk factors*. The contract type risk factor focuses on the degree of cost risk accepted by the contractor under varying contract types. The working capital adjustment is an adjustment added to the profit objective for contract type risk. It applies to fixed-price type contracts that provide for progress payments. Though it uses a formula approach, it is not intended to be an exact calculation of the cost of working capital. Its purpose is to give general recognition to the contractor's cost of working capital under varying contract circumstances, financing policies, and the economic environment. This adjustment is limited to a maximum of 2 percent.

(b) *Risk factor values and calculations*. A risk value is assigned to calculate the profit or fee objective for contract type. A contract length factor is assigned and applied to costs financed when a working capital adjustment is appropriate. This calculation is only performed when the prospective contract is a fixed-price contract containing provisions for progress payments.

(c) *Values: Normal and designated ranges*.

Contract Type	Note	Normal value (Percent)	Designated range (Percent)
Firm-fixed-price, no financing	(1)	5	4 to 6
Firm-fixed-price with performance-based payments	(6)	4	2.5 to 5.5
Firm-fixed-price with progress payments	(2)	3	2 to 4
Fixed-price-incentive, no financing	(1)	3	2 to 4
Fixed-price-incentive, with performance-based payments	(6)	2	.5 to 3.5
Fixed-price, redeterminable	(3)		
Fixed-price-incentive, with progress payments	(2)	1	0 to 2
Cost-plus-incentive-fee	(4)	1	0 to 2
Cost-plus-award fee	(4)	.75	.5 to 1.5
Cost-plus-fixed fee	(4)	.5	0 to 1
Time-and-materials	(5)	.5	0 to 1
Labor-hour	(5)	.5	0 to 1
Firm-fixed-price, level-of-effort, term	(5)	.5	0 to 1

(1) *No financing*, means that the contract either does not provide progress or performance based payments, or provides them only on a limited basis. Do not compute a working capital adjustment.

(2) When progress payments are present, compute a working capital adjustment.

(3) For purposes of assigning profit values, treat a fixed-price redeterminable contract as if it were a fixed-price-incentive contract with below normal provisions.

(4) Cost-plus contracts shall not receive the working capital adjustment.

(5) These types of contracts are considered cost-plus-fixed-fee contracts for the purposes of assigning profit values. Do not compute the working capital adjustment. However, higher than normal values may be assigned within the designated range to the extent that portions of cost are fixed.

(6) When performance-based payments are used, do not compute a working capital adjustment.

(d) *Evaluation criteria*. (1) *General*. The contracting officer shall consider elements that affect contract type risk such as—

(i) Length of contract;

(ii) Adequacy of cost projection data;

(iii) Economic environment;

(iv) Nature and extent of subcontracted activity;

(v) Protection provided to the contractor under contract provisions (e.g., economic price adjustment clauses);

(vi) The ceilings and share lines contained in the incentive provisions; and

(vii) The rate, frequency, and risk to the contractor of performance-based payments, if provided.